Bruce Bond: Ladies and gentlemen, we have been looking forward to this event so much for a long time. Let's get started. John, the floor is yours.

John Yemma: Well, thanks everybody for coming out tonight. I see we had a little bit of a snowstorm but you all made it. I think that's great. This is a little different. You've seen a lot of debates. You see them on TV. You've probably gone to them in person. It's a political year. You're gonna run into them all the time. This is different because we're using a format in which we're trying to understand the positions that sort of the – the position on the left and the position on the right. And then come to some sort of agreement. And, Kraft, our facilitator, will help us through this.

Now when I take you through the document that we're gonna be filling out, you'll see this as Kraft is working on it. And it may seem as though you're missing something at first, but just bear with us and I think you'll see that it proves that we can actually establish positions and establish facts pretty well.

The subject is tax reform. And I think it – there are plenty of reasons for tax reform. There is the question of, as we know from just the popular media right now, there's the question of fairness. And then there's the question of economic stimulation. The question of whether the tax burden's too high or the question of whether the economy is so complex that maybe you need the kind of complexity that is within the tax code.

So we're trying to reach a point where we understand the tradeoffs between fairness and lower tax rates. And fairness is not just an esoteric term and tax cutting is not just a philosophical term. But as taxpayers, which we all are, I think we all have a vested interest in understanding and in wanting to have a simpler way when April 15th comes along of dealing with taxes. I think it was Will Rogers who said that the tax code has made more liars out of Americans than even golf has made.

So it's clear that people want change. And it's clear that we need some kind of change given the deficit and given the question of fairness.

So I thought first we would go to Art and Jared, and in about a minute each just give us a high level view of where you think we are with tax reform and what philosophically we should be striving for. Jared, you first.

Jared Bernstein: Okay. Thank you very much. And it's great to be here. Don't count this against my minute. It's great to be here and to try to find common ground, particularly with my friend Art Laffer. As I always say, I disagree with Art on a lot of things, but I enjoy his company more than a lot of people I agree with. So it's great to be here tonight.

I want to just start out with a couple of, I guess I would call them, almost definitional thoughts in how I think about this question. I don't always like the way we talk about taxes. We talk about the tax burden. We talk about the tax liability. We talk about taxes almost exclusively in terms of costs. But in fact, taxes have benefits as well. Critical benefits to an economy like ours. And I don't want to be here tonight as Mr. Fairness. The fairness guy. Whereas if I'm ready to trade off efficiencies or benefits to our economy in the interest of fairness. I do, and you'll hear, amplify fairness as part of my understanding of these issues. But we are, as I speak to you, in an economy with aging demographics, with deep market failures borne of an interconnected global system with recessions, need I remind you. Recessions that need a safety net. Financial instability. Deficits in our public infrastructure. Middleclass wage stagnation and job losses. Extreme levels of income and equality.

Any one of those issues calls for an amply funded government sector. Something I believe, as you alluded to in the introduction, that we are at risk of losing if we don't get straight on this issue of raising the revenue we need to meet the challenges we face.

So in closing my opening statement, I don't want to think tonight about taxes as always distortionary burdensome liabilities. All costs no benefits. I think we have to appreciate the role that taxes play, that an amply funded government plays in an economy like ours today.

John Yemma: Great. Art?

Art Laffer: Thank you. I want to second Jared's. I enjoy being Jared enormously. We've done this several times now in three –

John Yemma: Could you hold the microphone?

Art Laffer: Sorry. Excuse me. You know coming – well, you know you do that. Coming over here this evening, you know was cold and chilly. You know it's been really warm for quite a while and I noticed a lot of the trees up there were already thinking it's spring. With this cold snap I saw some of them froze their little buds off.

[Laughter]

I had to get a giggle out of you. Tax codes. I mean tax codes, yes, you are here to raise the requisite revenues to fund government. That's true. But all taxes are bad. Some are worse than others. The role of taxation, in my view, is to do the – collect the requisite revenues in the least damaging fashion to the overall economy. I do agree with fairness. Fairness is very important. But fairness has to have an objectivity to it. And if you make ten times as much as I do, you should pay ten times as much in taxes as I do. I think that's perfectly fair. Perfectly correct.

And when you realize that in taxes, and you think of there are two types of incentives in this world. They're positive and they're negative. By way of illustration, if you beat a dog, you know where the dog won't be, but you have no idea where the dog will be. If on the other hand you feed a dog, you know exactly where the dog will be. Taxes are like beating them. You know exactly what people will not do. They will not report taxable income. But what you don't know is how they won't report their taxable income. They'll use evasion, avoidance, underground economy. They'll go out of work or they'll move to a different location.

So what you want to be really careful is that you don't destroy the ultimate engine of fairness, which is jobs. Output and employment. To me, the best form of welfare, Jared, is still a good high paying job. And economic growth is the one place where taxes really matter.

John Yemma: Okay, we'll come back to both of these points as we go. Let's first go to, Gail. Gail has covered Congress, as Bruce was saying, for a number of years. And understands – she's gonna give us the reality check throughout. What will – as we talk about reform, as we start to move toward some ideas, what's the policy reality here? And I thought maybe, Gail, you could just give us off the top of your head in a couple of minutes where we are with the question of tax reform and whether in this year or any year given the way Washington is, you can expect to see any movement.

G. Russell Chaddock: Well, the nice thing about talking about Congress is that you can immediately start and say, it's broken. And no matter what side you're on, Republican or Democrat, you'll quickly agree. Now there are iconic moments in Congress. My favorite was during the

Clinton impeachment trial where the Senate – the House was clearly going to impeach. The Senate got together. Now they could have impeached him. They got together in the old Senate chamber where Calhoun and Henry Clay and Daniel Webster had spoken. And they shut out the press. Good start. And then they shut out the staff. Another good start. And senators just talked to each other.

And it's interesting. There are a lot of senators who've written memoirs about this. And you can look it up in the index and go to that point and they all say exactly the same thing. That in the gravitas of that room and that moment, everything changed. They began talking and thinking like statesmen. Even though the Republicans could have impeached this president, they decided not to. And it's that iconic moment that Washington looks for hopefully. And it has shown up from time to time.

Welfare reform. The Reagan tax cut. I'm already running out of examples. I have to look down –

[Laughter]

Social Security in 1983 there are some. Clinton/Gingrich. Another example. And then we come to Obama/Boehner. Now this could have been an iconic moment. And I think that was a lot of the press coverage about it. I, myself, wrote a number of stories suggesting that there was a real possibility for a grand bargain here. And yet in the end the debt ceiling increase went right up until the last minute, right up until the first ever default on the national debt, into a downgrade of the US bond rating and setting up a set of kind of Rube Goldberg moments that never actually worked out either. Such as the super committee that turned out to be not so super. And now we're heading into a year to try to figure out whether even the mandated cuts that came out of that deal will come about.

Well, why is Congress so dysfunctional and why is it so hard to do even the simplest thing? I think it comes back very clearly to a sense of culture and public trust. Public trust in Congress hit an all-time low on Wednesday. Ten percent of people trust Congress to do the right thing. And it has to do with the fact that there seems to be so much brinksmanship and an inability to cross party lines. And that the politicians themselves don't believe that the kind of exercise we're going through tonight will be good for them or will produce anything of value.

Politico, I'd say the hottest new media outlet on Capitol Hill, wrote a big story the day after I agreed to do this. Which had one great line in it. It said, Washington is no longer the city of the splittable difference. Why? Because if you go through the exercise we're about to do tonight and you wind up in the middle, you're kind of like in the middle at Verdun. Where they're firing from both sides and the person in the middle is the most likely not to be reelected. People take Tea Party freshmen for example, look back on all those years of grand bargains and they say, what did it produce? Unsustainable deficits. A welfare system that cannot be sustained either. Health costs that are out of control. Coming to agreement in the middle is going to only spend more or become even less sustainable.

So what we really need to do is to commit these politicians in advance to pledges. Now the big one is on the Republican side. In 1986, not coincidentally the year that the Reagan tax cuts kicked in. I'd like to make a little footnote here though. Reagan didn't just cut taxes. He also raised them. As did Herbert Hoover. The only president in recent memory who cut taxes and didn't raise them was President Bush the second.

And one of the reasons I think, and as I talk to members of Congress that are on the Republican side overwhelming committed to this tax pledge – and I'd like to just spend two seconds talking about it because it's going to cover a lot of what we talk about today. It defines whether there even is a middle.

This tax pledge has two elements. One, do not raise tax rates. And the tricky one is the second. Do not cut tax breaks no matter how egregious. Unless they are offset by cutting tax rates somewhere else or other offsets. In other words, whatever you do on the tax break side, and you know tax breaks are now a trillion dollars a year. It's about as much as you take in in disposable income. We're talking about a huge sum of money here. Whatever you do to tax breaks has to net to zero.

Now as long as Republicans hold to that pledge, there is no middle ground. There's nowhere to go on revenue. That's –

John Yemma: So, Gail, why don't we pick up now and then we'll come back to that as we go through? We'll come back to sort of the political reality checks as we –

G. Russell Chaddock: Excellent point.

John Yemma: Okay. She's showing you how easy it's gonna be. So that's –

Jared Bernstein: Could I interject a factual point. President Obama, over his term so far, has not raised taxes yet has cut taxes quite deeply. Now he has presided over legislation that raises taxes later. That's true. But in terms of a president who has cut your tax bill, President Obama ranks right up there with Bush two. Just a factual point.

John Yemma: Art?

Art Laffer: I'm just gonna the one, two you mentioned there. I love them. I mean I, for example, found a tax compromise really wonderful was Simpson Bowles. And I found Rivlin Domenici was wonderful. I mean in lowering rates, broadening the base. You know details you can argue about. The one I loved, and you mentioned it, was the '86 tax act. I mean the '86 tax act, let me tell you what happened.

We dropped the highest tax rate in America. Tax rate. From 50 percent to 28 percent on those with the highest earnings. You all with me on that? That a big enough cut for ya? But what that also did was it raised the lowest rate. It raised it from 11 percent to 15 percent. First time in US history a tax bill actually cut the highest rate and raised the lowest rate. Now they got rid of a lot of deductions, exemptions, exclusions. So it was revenue neutral or close to it. Maybe a little bit positive. I don't remember that.

But guess what the vote was, people? In the Senate. Come on. Ninety-seven to three. Simon, Belcuore and one other senator voted against it. Ninety-seven senators for it. Let me tell ya, Alan Cranston, my former senator Al Gore. You had Bill Bradley. Not known as a right-winger. You had – what was his name? From Delaware. Joe Biden voted for it. Not only Joe Biden but you had Teddy Kennedy. I mean this was the day when we had serious statesmen do things in a pro-growth fashion because they understood the supply side economics works and that we all –

[Laughter]

But it is serious. I think we all are here to do that. I would go for Simpson Bowles any day of the week –

Jared Bernstein: Which by the way, raises about 2 trillion in revenue.

Art Laffer: I know. We can argue about the little bit here or there. Let me just say, I want to raise taxes. I really want to raise taxes. And I'm not joking on that. But I don't want to raise tax rates. What I want to do is create jobs, output, employment and production so that everyone pays taxes and they pay a lot more taxes by creating growth. You can't balance a budget on the backs of the poor. The unemployed.

John Yemma: How about if we launch into this and you guys will still be able to make these points, because you've done this before and you know that you can break the mold any time. That's the way you always do it on TV, right?

So, Kraft, let's go through this document. Basically, you know it's a little wonky but bear with us. On the left I'd say it's really the tax rate cutting side of things. That's really Art's side of things. And on the right, just on paper here, is the – represents the other side. Which is essentially to look at what revenues do for the, and what tax revenues do for the economy and for government.

And then down the left we're gonna march through three main points. We're gonna look at the current tax realities and the impact on the economy and on society and on the budget. And then we're gonna go look at tax reform. And we're gonna – through the lenses that Art and Jared have, we're gonna see if we can reach common ground on deficit reduction, fairness and economic growth. Pretty good areas. No disagreements there probably. And then we have to think about implementation. And this is where Gail's gonna help us a lot I think. You know can we be both fair, and I realize fair is a loaded term, but fair and pro-growth? Can we stimulate the economy and improve the budget balance?

So that's really what we're seeking here. And we're looking at what are the impediments and we know that they are considerable. Gail I think has outlined those.

So let's go to – here we go. On the first one. We've gone back to the beginning here. We're looking at the key areas. The realities of tax reform right now. And on the left we've begun to fill these in using the staff of the Christian Science Monitor and also with check offs from Jared and Art. On the left you've got, you know lower tax rates stimulate private sector growth. It's a truism about tax cutting. Lower corporate tax rates render the US more globally competitive.

And then on the right you've got targeted spending and investments stimulate growth and demand. Right. That's the stimulus bill and that kind of thought. And also that government spending is essentially an investment in some ways. I mean building super highways or green technologies. Our massive projects help to build an economy that's more competitive with say China and Japan which do that all the time.

And then you have this problem of revenue shortfalls lead to unsustainable debt levels if you don't actually match those.

Jared Bernstein: So can we now comment on these?

John Yemma: Sure.

Kraft Bell: Here's what we're gonna do. We're gonna go all the way through this so people can see what the key points are. And then we're gonna come back one by one and we're gonna have these things right back up there. You can comment on them. And hopefully we can get to common ground between them. So we want to go through all three of the sections.

John Yemma: Okay. We're gonna go to the next one. So then you look at the impact on society. If you lower tax rates it boosts free enterprise. That's a good thing in America. Job creation and productivity. And also if you have uniformly lower rates you could broaden the base. You have more people invested essentially in this country as taxpayers. More people paying taxes, more people then thinking about where their money goes.

And on the other side you have targeted taxation, which is closing the income gap between, and helping to ameliorate the class divide that we hear so much about. And then eliminating subsidies on corporations that don't need them. Maybe that removes economic distortions and helps the middle class.

On to the next one which is impact on the budget. So lower tax rates should – they initially boost the deficit probably because you're cutting back on taxes. But in time this is called I think the Laffer Curve? In time they –

Art Laffer: My profile.

John Yemma: They boost revenues. And they unleash a kind of a creative boom in the economy. And increasing the tax base controls the deficit until the higher revenues kick in. Now on the other side you've got stimulus spending temporarily raises the budget deficit. Right, it's going to. It's happened. But once it ends the impact on the debt is minimal. And if you can't achieve a sustainable budget without new revenues, then we should start by increasing taxes on those who can afford it.

Okay. And then on the goals of tax reform we're looking at deficit reduction and fairness as two of the big goals. Deficit reduction on one side is about stimulating growth by cutting taxes which nets new revenues. On the other side is stimulating growth by investing and essentially broadening the base and, therefore, taxing those who can afford it. And in the fairness area, you know there's a fairness argument on the tax cutting side too. Which is you reduce the opportunities for tax avoidance by cutting back on the way, and actually getting more people into the economy. That's gotta be a fairness issue. And then you end preferential tax treatments for different types of income, like the earnings of hedge fund managers. So.

Jared Bernstein: Just to pull an example out of the air.

John Yemma: Just one. Okay. And then on – we're looking at economic growth. So a flat tax should insure that everybody pays their proportional share. I think that actually goes with the earlier one. Economic growth is boost entrepreneurship and strengthen global competitiveness. And on the other side it's address market failures both through stimulus and recession and investment where the market's inefficient. So that's that investment argument again.

And then finally, you know rethinking and implementation. How can we make it both fair and pro-growth? And here, you know we may not get through all of this, but I think we're gonna look at whether we can get a simple fair tax that stimulates entrepreneurialism and helps the economy across all economic strata. And on the other side, it's can we get productive government backed initiatives? Broad enough that they don't play favorites or create an expectation of continual funding. Which is the argument against the entitlement society argument.

How can you stimulate the economy and reduce the deficit? You really want to trigger on one side supply side growth in a way that attacks the deficit in a reasonable period of time. And on the other side, perhaps government investments with a strong rate of return and a sunset provision and give you offsetting cuts of new revenue.

So we've gone through all of this. And I think maybe we want to then move on to the – we've got one more page here.

Jared Bernstein: Before you go to the next page, would it be okay – I don't want to bust your thing here, so just put me – if you go back to the beginning. I just want to just make sure we have a chance to – I don't think we're gonna get to all this. So I want to make sure I have a chance to comment on some of the critical things you –

John Yemma: I'll tell you what, we'll go back to the beginning and we'll just start at the beginning.

Art Laffer: I'd love to hear Jared on some of these.

John Yemma: Give me one more page.

Jared Bernstein: Sure. Sure. Go ahead. Take another page.

John Yemma: I'll stop the filibuster event. Okay. The impediments. If we go flat we can also lose deductions, like mortgage interest. We eliminate subsidies. And what do we about capital gains taxes? Estate taxes. Unearned income so-called. And then on the other side, if we stay progressive can we cut entitlements significantly to bring the budget into balance and how do we avoid a culture of dependency? Okay.

Art Laffer: You're on.

Jared Bernstein: Alright. So here's the thing that cuts through – I didn't mean to interrupt. I'm sorry. I'm chomping at the bit here. Because here's the thing that cuts through all of this, and it's a fundamental disagreement that Art and I have. And I think the evidence supports my views here. But we're gonna – you'll hear Art maybe disagree or maybe finally see the light.

Running through all of the stuff on, I guess it's red there. The side about lower tax rate simulating all that, is something that economists call elasticities. An elasticity in economics is the response to a change in the tax rate. And the thing that I find deeply problematic about supply side economics is it massively exaggerates the responsive to tax changes. The idea that if you tweak a tax this way or that, you're going to see these kinds of growth effects that replace the lost revenue, that lead to booms in the economy, that get people back to work, that get investors coming off the sidelines. Not only does the theory not support that, in ways I'd be happy to articulate. But not only does the theory not support that, the theory says it could go either way. But the evidence doesn't support that.

Probably case one would be comparing the 1990s with the 2000s. The 1990s we did exactly the opposite of what supply side tax policy would suggest. And we had a much better economy, both in terms of job growth, stock market, by the way, in equality, jobs for middle class people, even low income people. Poverty fell more in that –

Art Laffer: Let me respond. We all agree with the 90s.

Jared Bernstein: And the 2000s, where we followed a supply side playbook, exactly the opposite. The worst economic business cycle in our history.

Art Laffer: I think we both agree with the facts about the 90s and the 2000s. There. Now let's talk about the economics. I voted for Clinton twice. And I did not vote it because I thought he was a left winger. Clinton, when he came into office, pushed NAFTA through Congress. Against his own party, against the unions. Clinton got rid of the retirement test on social security, if any of you remember that. Clinton signed into law welfare reform that you actually have to look for a job to get welfare. Now there's a concept. Clinton also reappointed Reagan's fed chairman twice. Clinton signed into law the largest capital gains tax rate reduction in our country's history.

[Clapping]

And also – which by the way, exempted owner occupied homes from capital gains taxation. But most of all, ladies and gentlemen, why I voted for him, he cut government spending as a share of GDP by more than the next four best presidents combined. Now government spending is taxation pure and simple. That's what it is.

Now let's go to Bush. Let's go to Bush and Obama. And I'll put them together cause I think they're very similar. You start off with the what happened in 2007 with the stimulus on the agricultural bill, the housing bill. Then you had Larry Summers 600 bucks per capita tax rebate. You had AIG. You had TARP. Seven hundred billion there. Then you nationalized Fannie Mae, Freddie Mac, the 862 billion there. And then the deficit's beyond. That is a tragedy of over taxation. And that is why the economies performed differently. My view. And we do agree on the facts. I thought Clinton was one of the best presidents the United States has ever had. Second only to you know who. Ronnie. Excuse me.

[Clapping]

Now let me if I can, on the last one. On the sensitivities. These are numerical issues. It is not a theoretical issue. He's gonna argue the income effect. I think you are.

Jared Bernstein: You're right. There's a substitution effect which you –

[Cross Talk]

Art Laffer: The point of it is, the income effects, if any of you remember your Slutsky equations. The income effects on the economy always sum to zero. You know whenever you get a tax rate change there are those –

Jared Bernstein: Explain the – you should just go with it.

Art Laffer: Sure. I'll use the substitution effects are when you – I mean, excuse me. The income effects are when you get a change in income that results from a tax change. For example, if I get my tax rate lowered. And I'm a big earner. I will have an effect of having more income with the exact same amount of work as I did before. Now with that more income I may well want to choose more leisure. And buy more leisure. Which means that I may or may not work harder. But if everyone in the society chooses more leisure there'll be less transfer payments and those people will have income effects that move in exactly the opposite direction.

I'm gonna give you Val Rah who brought it into economics. His example. If the price of apples rises, it is very true that apple growers will be wealthier, they'll have higher incomes and they will spend more. But it's equally as true if the price of apples rises, apple consumers will be poorer, they will have lower incomes and they will spend less. These two effects offset each other. By the hour, by the day, by the week, by the month, by the year, to the 5987th decimal place. Tax rate changes do not have a net income effect period. Nor do transfer payments have a net income effect.

But they do have substitution effects that always work in one direction. And you can see that taken to the argument absurdum where we tax everyone in society 110 percent of everything they earn. So that every time you go to the office instead of getting a check you get a bill. How long are you gonna work? It's clear that output will fall. It's a continuum throughout the whole process.

Jared Bernstein: So I think that's a canard. Because, you know I think it's absolutely the case –

Art Laffer: Is that a type of duck?

Jared Bernstein: It is, I think. I was actually careful in my presentation to say that the supply siders way exaggerate tweaks in the – I think I used the word tweaks. What you're talking about, for example, the president's proposing to take the top income tax rate from 36 percent to 39.6 percent. I'd stipulate maybe this will even get in the middle column, but I'm afraid maybe not. I'd stipulate that that won't have any effect on labor supply that you could pull out of any reasonable dataset. That, to me, the idea that conservatives would line up against a tax rate of that magnitude based on supply side imagination I think is a very unfortunate one.

Art Laffer: Let me just imagination here. You know the real problem with tax rates is not the supply side effects of people working more or investing more. The real problem is with you have – you can use if you're wealthy you can evade, avoid, otherwise not report taxable income. You can use lawyers. You can use accountants. You can use tax deferred specialists. All sorts of things in the tax codes.

For example, I did a piece in the *Wall Street Journal* I think about four or five weeks ago on Warren Buffett. And his whole wealth, his increase in unrealized capital gains. Do any of you know what the tax rate is today on unrealized capital gains? It's zero. He is worth 50 billion dollars and he's never paid a penny on that 50 billion dollars which is unrealized capital gains. If he gives that to the Bill and Melinda Gates Foundation or to his son's foundation or his daughter's, it will never see a tax. That's grotesquely unfair. My view. I think we should have a low flat rate tax on all income so you don't have places you can slither to. I mean, gosh, sakes, you really want to make it.

I moved from California to Tennessee. I mean I moved. I literally did. Because of taxes. You know there is no state income tax in Tennessee. I paid for my house in my first year's tax savings. I mean it's fun having a house for free. And especially when they're not harassing.

So I think it's not just the labor supply, which is where all the Keynesians have always argued about it. It's also on using the lawyers, accountants, tax deferral specialists. That's where the real dodges come.

Jared Bernstein: So I think that this, again, I mean the idea that we can never raise taxes because people will evade taxes is far too accepting of tax evasion behavior. And I think, in fact, our economy has become much too compliant in that regard. I agree with you that simplicity, we absolutely need it. And that should be right there –

Art Laffer: Middle ground. Middle ground.

Jared Bernstein: That's right. But operationalizing that isn't as easy as it sounds.

Art Laffer: Oh, you and I could do it.

Jared Bernstein: But, again, if you actually enforce tax law, then tax evasion is something that's truly punishable. I would imagine that if you started to actually really put some people in jail for the extent to which they evade the rules of our tax system you'd see a whole lot less tax evasion.

Art Laffer: Can I ask you about tax evasion? I mean people will tax evade and they always will and they'll try. And, of course, we should have severe penalties for tax evasion. I mean it's part of the social contract we all have. But what you want to do is have a tax code that's fair, that's simple, that's easy to understand. So that you don't have this fear when you get a letter from the IRS. You know. And if you have a low rate flat tax, you won't even have to file a tax return.

Jared Bernstein: Let's bring that to cases. How about we close the carried interest loophole?

Art Laffer: Well, if you want to do it piecemeal I'd be glad to do it piecemeal with you. But let me –

Jared Bernstein: Let's just get this on the table. It's a simplicity thing. I think that that's an example of something here that you are saying you're for. So I'm not trying to be annoying. I'm just –

[Cross Talk]

Art Laffer: No, you're not annoying at all. You're loveable. But let me just say that I really find it very hard to cure one little thing here, one little thing there. What you really want to do is have a broad based tax like I did for Jerry Brown. Now I don't know if any of you remember Jerry Brown's campaign. I wrote his flat tax. His 13 percent flat tax if you remember. By the way, he was a Democrat. Coming into the primary he almost beat Bill Clinton.

What you do is have two flat taxes. One on business net sales and one on personal and adjusted gross income. Very few deductions, exemptions or exclusions of any sort. And if you did that, you could have a rate that is static revenue neutral. At full employment. Now static. At 12 percent or less. And so if you get your income – if you get 100 bucks income, they'll just give you 88 bucks. You won't even have to file a tax return. Now if you mow your neighbor's lawn for ten bucks, you will have to send in $1.20.

John Yemma: So let's stay on flat taxes for a while.

Jared Bernstein: Sure.

Art Laffer: That's where I – and simplified so you don't go to jail.

Jared Bernstein: Okay. So a couple things on flat taxes. Every conversation about tax reform ends with some economist saying, we should have flat tax rates. And the reason is because it's actually a good idea.

Art Laffer: There we go.

Jared Bernstein: I mean you need to implement them in such a way that folks at the lower end of the income scale don't face the same tax rates as those at the higher end. You have to be careful not to tax the basic consumption for people. It's actually not hard to design that. You can design a flat tax that kicks in at some higher point in the income scale and that accomplishes the goals I mentioned.

The problem is, and here Gail may have some input. The problem is it's – I don't want to say it's a waste of time. I don't think it's time well spent for yet another conversation of tax reform to end on a suggestion that just ain't gonna happen. It hasn't happened ever before. It's not gonna happen probably in our lifetimes I'm sorry to say. So I'm afraid that what we have to do in the real world is start to hammer away at some of the things that are infecting our tax code in ways that you and I could probably agree.

So the fact that you pay 15 percent on what's called carried interest. The fact that you pay 15 percent if you're a hedge fund manager on capital gains from hedge funds that you don't even have any risk capital in seems to me absurd. This is the Warren Buffett problem but Mitt Romney recently surfaced with the same issue. Seems to me absurd when you've got other people paying on their wage income 35 percent, perhaps, I mean 36 percent, perhaps going up to 40. So it seems like we could agree on that.

Art Laffer: I don't think we disagree on –

Jared Bernstein: Okay.

Art Laffer: Pay the same. But you've got to include all forms of income. I mean you really do have to include it there.

Jared Bernstein: So this is a big form of agreement for the people right in the middle column there.

Art Laffer: I think it is a great form – and you want to have a – now I will use Jerry Brown's quote here. When he, Jerry Brown, when he did the flat tax. Made it start at dollar one to dollar N at the 13 percent. There was no change in rate. That's what he did. And when he was asked about the poor he said, can you tell me what the benefit of a tax deduction is to someone with no income? Maybe I missed that in econ 1, Jerry used to say.

Jared Bernstein: I'm think of 15, 20K.

Art Laffer: Well, but what you want to do is, see then it all of a sudden gets two different categories, which then makes it you can't get it just withheld from your firm and you have to file a tax return. That's the problem with it. I would much rather use government spending to help a poor person than I would using taxes. Because as I tried to say at the beginning, you know if you feed a dog you know where the dog will be. You can really do a lot more to help –

Jared Bernstein: Okay. But I just want to identify for the audience. I think we narrowed in on a really, really important key issue of tax reform. Let's see if we agree on this the way I'm gonna say it. You shouldn't favor any kind of income.

Art Laffer: That's right.

Jared Bernstein: You shouldn't favor any kind of – you shouldn't favor this income because it comes from this guy in this sector and this gal in that sector or it's manufacturing versus energy. That creates a level of complications that just I think –

Art Laffer: Hundred percent together.

John Yemma: Art, do you agree on unearned income too? Do you consider that income? In the same sense.

Jared Bernstein: Yes, he does.

Art Laffer: What do you mean by unearned income?

John Yemma: Like capital gains.

Jared Bernstein: Capital gains. Dividends.

Art Laffer: Oh, sure. Sure. But it's only taxed once. You know you raise the basis then for the next time. And if it goes down, you give them a rebate back for it. In other words, it's considered negative there. If you have a capital loss, you get your money back the next year. So exactly like it cause then it's a negative income.

But that's the way you really want to go is that flat tax and that.

John Yemma: Okay. Let me turn to Gail. Gail, it looked like you wanted to get in on this. Do you sense – in listening to this, do you sense that there's any point of – I mean we've reached some degree of common ground with flat taxes. But what about implementation?

G. Russell Chaddock: I was gonna ask Jared why he wrote off so quickly the idea that Congress could do something as apparently –

Jared Bernstein: Well, you started out by saying Congress can't do anything because they're dysfunctional and I'm agreeing with you.

[Laughter]

These guys are having trouble arguing about keeping the lights on. So.

Art Laffer: But that's this Congress.

Jared Bernstein: Yeah, no, I think it's –

Art Laffer: In '86 we did do that. I mean that was the whole dream was then a flat tax. It was Bradley/Gephardt, it was Kemp/Kasten. If you remember, I mean that was the dream, bipartisan dream.

Jared Bernstein: That was not a flat tax.

Art Laffer: But it was getting there. I mean never let the best be the enemy of the good.

Jared Bernstein: I'm with you on that.

Kraft Bell: What is it – let's just stick with this. What is it that creates the dream? You know in change one of the things that happens is you have a burning platform. Alright. And everybody says, we gotta jump. Alright. The other one is we have a dream. You know we go for a dream and say, let's go for that vision. So what is the burning platform or the dream? Cause we've had a burning platform here for about five years.

Art Laffer: That's right.

Kraft Bell: And it hasn't gotten us anything. Okay. And the burning platform is five years out or ten or 30, but people aren't responding. So the question is what –

Jared Bernstein: Let me try to answer that and also address Gail's question. You have heard myself and Art Laffer, who are really coming from this from very different places, agree on significant new revenue. Okay, Gail. I mean you heard that.

G. Russell Chaddock: Heard it.

Jared Bernstein: He said Bowles Simpson. Bowles Simpson raises something like 2 trillion in revenue. Now you work the Congress. The idea of that kind of revenue, or any kind of revenue, is – doesn't that strike you, at least with, I don't know, just this group, but certainly probably this group and the group we're gonna be looking at for a while, as a heck of a reach? Am I wrong? So anyway, you can answer that in a second. But I'm just saying the dream. The dream is that we have a simple, easy to apply, fair tax code that raises revenue so that we can have the government we need, desire – we can argue about what that is. The government that we need and desire and it's functional and it doesn't leave debt burdens on the future. I think it's pretty simple.

Art Laffer: Yeah I mean what you really want to do is you do two things. I mean if you create a low rate, flat tax in the system there and you get the economic growth, you'll reduce the need for a lot of government spending because if you have people that are fully employed and are making good money there's no need for a lot of the transfer payments there. I mean that's there. By getting rid of the deductions, exemptions, exclusions you'll get all these people that are wasting their time trying to figure out the dodges and loopholes and things around it. I mean if you saw my piece in the *Wall Street Journal* I guess two months ago where I looked at the total costs of just filing your tax returns. In 2006 that number came out to 430 billion dollars just to file out of pocket costs. I mean that's out of pocket.

What you want is a tax code that the people pay what the government collects. So that there's not all these wasted resources. This is what we're all talking about. And then you'll have a really fair system. A fair system is one that allows the system to really thrive and prosper.

John Yemma: Okay.

Art Laffer: And by the way, it was Obama who didn't push forward on the Simpson Bowles. And it was Obama who didn't push forward on Rivlin Domenici. Ask Alan or ask Bowles. Either one of them.

Kraft Bell: I think the question is, it's like if we get into the blame side of this it doesn't help us a whole lot.

Art Laffer: No, it doesn't.

Kraft Bell: So I think the question is, what would it take in order to get people to say, this is the direction we need to go? So you've given us several examples where things could have happened and they didn't. Gail, you talked about the fact there was this, we had, you know Boehner was there. The president was there. It seemed like something was in the grass. But what will it take in order to bridge that gap? What can you recommend? What –

Jared Bernstein: I think it will take a new set of people in Washington. I really do.

Art Laffer: I think that's true too.

Jared Bernstein: I mean I think that many people have been –

[Clapping]

Art Laffer: From the top down.

Jared Bernstein: I think there have been –

[Laughter]

I'm thinking about the Congress.

Art Laffer: I know you do.

Jared Bernstein: I'm thinking about the Congress. You know there were people who were sent to Congress to block compromise in my view. And we cannot achieve the goals that we're trying to talk about today if blocking compromise is what wakes you up in the morning.

You know probably the worst thing I heard this year, and I heard a lot of bad things, is when Senate Leader Mitch McConnell said, Minority Leader Mitch McConnell said, you know our main goal this year has to be defeat President Obama. This is in a year with 8 plus percent unemployment and budget deficits.

Art Laffer: I think we can agree on this too. I mean I think it is really dysfunctional and it doesn't do anything to be blaming either Mitch McConnell or Obama. Both of them. They both get frustrated. They sometimes say things they shouldn't say. We all have done that in our lives. But I think for you and me, Jared, really the point is here to point the way for it. And on some of these areas of grounds I'd be glad to do an editorial with you and me together on that.

Jared Bernstein: That's an interesting idea.

Art Laffer: Ah.

John Yemma: Interesting in *The New York Times* today there was a *New York Times* poll. And in interesting article. But *New York Times* poll that said 70 percent of the people polled said that they would support higher taxes. What it didn't say is on whom. Although it did say –

Jared Bernstein: On the other 70 percent.

John Yemma: It did say that 50 percent of Americans – 56 percent of Americans support cuts in Medicare and social security and that 85 percent want to see an increase in taxes on the wealthy.

Jared Bernstein: Yeah. So let me talk about that for a second. Cause I don't want to get too far away from the idea of progressive taxation. I do believe that we need a progressive tax code. I think that there are fairness issues there. I think it's very much established in advanced economies across the globe that those who have more should contribute more. So I think that that – I think that has to be done in the context of as flat as possible, as few loopholes as possible. But I have no objection at all to a tax code that has graduated rates that increase as income goes up. And that's probably a source of –

Art Laffer: Can I ask you a question on those who have more should pay more? I agree with that totally. In fact, I thought I'd said that if you make –

Jared Bernstein: I think you did.

Art Laffer: Ten times as much as I do you should pay ten times as much in taxes. But that is not progressive. I do not – I think it should be proportional. And that those who make a lot more should pay a lot more. But not proportionally more. That's where I – and I think you've really gotta worry about the very wealthy having the highest tax rates because they're the ones that can use the lawyers, accountants, economists and all that stuff to get around it. And also they're the people who hire the other people. They're the people who do the investments where the jobs are. You really can't – you can't love jobs and hate job creators.

Jared Bernstein: Nobody hates job creators.

Art Laffer: But you can't go after them at higher rates.

Jared Bernstein: Again, I really do not – and I think there's a long empirical, not theoretical, empirical literature that supports this. You said two things and I fully agree with the first one. It is true that when you raise taxes on high income people they look for new ways to evade their higher taxes. I agree with you. But what they don't do is change their investment or job creation behavior. That I think, again, is just not supported by the evidence.

John Yemma: Gail?

G. Russell Chaddock: Well, if a change in the tax rate has a negligible impact on economic behavior, it does not have a negligible impact on political behavior. Raising taxes is death to politicians, especially on the Republican side. So we're heading into an election now where for the first time we're looking at unlimited individual and corporate contributions to campaigns in ways that cannot be tracked. And so given that climate, even taking the example you've picked, the 15 percent hedge fund rate, which is probably the least popular tax on Capitol Hill, there's almost no one that wants to publically say they support continuing it at that rate, do you think it's possible to get rid of that at this point?

Jared Bernstein: Not right now. I don't think it's possible to politically to raise revenues. And that would be a revenue raiser. And the president is going to promote to release a budget tomorrow morning and it's going to have 1.5 trillion I believe in new revenue. And I guarantee you that there are those on Capitol Hill who are already saying this budget is dead on arrival.

G. Russell Chaddock: They've already said it.

Art Laffer: Yeah.

Jared Bernstein: They've already said it.

G. Russell Chaddock: The Senate Majority Leader said he's not even gonna take it on the floor.

Jared Bernstein: The answer to your question is not right now.

Art Laffer: Couple things just here. Number one, I don't think there's anything wrong with people taking pledges if that's what they need to do to get elected. In other words, to hold a politician – really to hold a politician to his word is not something I find offensive in any sense of the issues there. So if people say, I will willingly sign a pledge, they should keep it. I mean that's what they should do.

I'm gonna disagree with Jared on the sense of taxes not having very major economic effects. I think taxes have been the primary cause of downturns in the economy. In my view, over the last 100 years, the income tax has been a debilitating killer of jobs, output and employment, because of changes in policies. Factually. That's my view or my interpretation of the fact.

Jared Bernstein: I mean I don't see how you would link that to, for example, the great recession, which was very much the outcome of a housing bubble.

Art Laffer: I totally do.

Jared Bernstein: Okay. Let's hear it.

Art Laffer: I don't think it's a housing bubble. I think it was the increase in spending that came about in the 2007 and 2008 which really caused this to crater. I think in the – I mean, you know –

Jared Bernstein: The average spending under Bush two was about 21 percent. Which was about, you're right, Clinton was a little bit lower. Reagan was a percentage point higher. So I don't think it's spending.

Art Laffer: Well, we can argue the –

Jared Bernstein: Twenty percent of GDP.

Art Laffer: I mean I think Clinton was one of the best presidents ever and I think the reason we had the boom there was because of his cutting spending so dramatically during that period. But I don't think the evidence supports the fact that taxes have minimal effects on the economy.

Jared Bernstein: So there's something where we have to agree to –

Art Laffer: We have to look at it –

Jared Bernstein: Agree to disagree.

Art Laffer: It's a much broader thing than five minutes of debate here but.

John Yemma: Okay.

Kraft Bell: Can we go back one step? Cause you started to get close to something. You started talking about pledges and whether they're significant or not significant, whether they should be made or not made. I guess the question is, if – how would Bowles Simpson have gone forward if there are pledges on both sides that they're not gonna agree to it? Did that –

Art Laffer: I think Bowles Simpson would not have passed as it stood unless they had an up or down vote. If they had an up or down vote I think it could very easily have passed. I don't know if it would have, but –

Jared Bernstein: I think, I very much differ on this pledges point, just so that should come out in the middle as far as I'm concerned. I mean I think the idea that there is this unelected guy named Grover Norquist who is so deeply –

[Clapping]

It's undemocratic. That that – that somebody like that would be so influential in such key policies. No, I don't think politicians should make those kinds of pledges at all. And by the way, it's very important to be dynamic about taxes. Sometimes you need to raise them. Sometimes you need to lower them. These pledges are completely insensitive to an actual business cycle.

Art Laffer: But that's true. But then don't make the pledge. If you make the pledge, then keep it. I mean –

Jared Bernstein: I agree with what you're –

Art Laffer: When you're talking about here, and if you don't want to make it, don't make it.

Jared Bernstein: So the way I view it, it's not Grover's fault. It's the fault of all the politicians who make the pledge.

Art Laffer: Yeah. And if they do make the pledge they better keep it. And when I look at the vote patterns here, when I look at how Obamacare passed or Dodd Frank passed. I mean it was 100 percent of the Democrats that voted with it all the way. It was like rote marching. You know very well that in a little private room these guys would not all agree from one party and all disagree in the other party. These are party mechanisms that have required them to behave just like Grover Norquist does it for the pledge, these guys do it in the things. I've gotten all these Democrat calls –

Kraft Bell: Let's shift roles. If you were in their shoes. The two of you. If one of you was leading the House. You know if you were now working on this, what would you say to each other that would start to bring this to a point where you could do something about it? Cause we know what doesn't work.

Art Laffer: I think that would be easy.

Kraft Bell: But what does work?

Jared Bernstein: I would really push for 1986 style tax reform.

Art Laffer: I would too. And 1986 was the best tax bill ever. Dropping the highest rate to 28 percent. Wahoo. I'll take it every day of the week and twice on Sunday.

Jared Bernstein: I will say one thing here's where I've, just to be clear where my colleague and I across the – we're – this is really important. And I think we kind of alluded to it earlier. I want to get back to it. I want members of the audience to be very aware of this. Because it may come up if we ever get to this kind of moment where we can actually have serious tax reform. We're gonna have a discussion about corporate tax reform in a couple of weeks I think when the White House releases some ideas about that.

I agree that we should broaden the base and I'm happy to lower the tax rate as part of that. But it can't be revenue neutral. We can't give away all of the revenue that we would get from broadening the base by taking the rate all the way – it's gotta be more than revenue neutral. We are now collecting 15 percent of GDP in revenue. We're spending 25 percent. Well, actually now I guess about 24, 23. So the difference, of course, is the budget deficit, which is 8, 9 percent of GDP. That's not sustainable. We all know that's not sustainable. It's a temporary matter having a lot to do with the great recession and the stimulus measures that have helped us get out of it. But you can't sustain that.

And so we have to collect more revenue. We have to cut the spending down. It has to be balanced. So there's no way we can do revenue neutral. We have to be revenue positive.

Art Laffer: Can I answer that?

G. Russell Chaddock: That, of course, is the heart of the pledge.

Jared Bernstein: Yes. That's why the pledge is completely –

[Cross Talk]

Art Laffer: If I can respond to this. I mean when you talk about revenue neutral, you can talk about revenue neutral of the static conditions they are now using static analysis. But, you know if you're talking about raising revenues, come on, help me. You can't balance a budget on the backs of the unemployed. You've gotta create jobs. And I'm all for raising revenues.

Now what we did with Jerry Brown's flat tax is we had it static revenue neutral at full employment. Which would be raising the rate to about 20 percent of GDP from 15 or 16 percent where it is today. That's what we did it back then. And that's the way I view Simpson Bowles is doing it in that same. So you gotta cut spending a lot more too.

Jared Bernstein: So let me interpret this. I think what you're saying for the audience. If I understand it correctly. Which is that you I think want to do dynamic scoring. You want to build in growth effects to your supply side tax cuts.

Art Laffer: Of course.

Jared Bernstein: Yeah. I'm wary of that. This is the idea that says –

Art Laffer: I'm wary of it too. But I want to do it.

Jared Bernstein: This is the idea that says we can cut taxes, the CBL will say no, you know this is going to lose revenue. But Art Laffer will say, no, it's not going to lose revenue because you're gonna have all these simulative effects from the tax cut. I haven't seen them and I wouldn't – like CBL, I really would be – I would tread very carefully about such dynamic scoring.

John Yemma: Did they not exist in the 1980s during the tax cut?

Art Laffer: No, there was no dynamic scoring then. Oh, but the revenue feedback that did exist. Oh, if you look at Marty Feldstein's study on what happened with the '86 Tax Act and how much more people reported an income for the same – I think it was 4,000 people he followed, Jared. Went through each of their tax returns before and after. Found it – not counting any of the secondary or tertiary effects which these guys then employed more people, they had all of that stuff happen. Hugely positive on revenues.

G. Russell Chaddock: Can I go back a minute to the tax expenditure side. This 15 percent and all the rest. People are very, conservative Republicans, freshmen, Tea Party Republicans, are very fixed on the tax rate. That is just set in stone. But in the year that I've talked to freshmen members, they're shaking on the bad tax break side. They're looking at some of these, as they get to know the tax code, some of these elements that they just think are indefensible. It was a very interesting hearing the Ways and Means Committee had last week where they brought a number of corporate heads together and they said, would you be willing to give up your tax breaks to lower rates? And just a little quiz here, if you eliminated all corporate tax breaks what could you bring the rate down to do you think and be revenue neutral?

Art Laffer: Really low.

Jared Bernstein: All corporate tax breaks? Bring the rate down and be revenue neutral?

G. Russell Chaddock: Mm hmm.

Jared Bernstein: So it's 35 percent is the statutory rate. Maybe mid-20s.

Art Laffer: Now let me give you one. GE pays no taxes at 35 percent. I will guarantee you they will not pay any less at 0 percent.

[Laughter]

So I will guarantee you that if you lower it to 5 percent you're gonna get more money from GE. Now that's one example. But that's the one because he – the only reason I mention GE cause, Jeff, I think is on your boss' panel. Isn't that right?

Jared Bernstein: Yeah, the competitive –

[Cross Talk]

Art Laffer: I'm just teasing. But you see what happens is that's not what you want corporations to do. You want them to do the investment income without consideration. You want the rates sufficiently low that they do business instead of doing tax dodges.

G. Russell Chaddock: This might actually be worth a common ground. I'm determined to have something on the yellow side here before I leave tonight. And this might be one of them. because I think when Simpson Bowles was just rejected by the White House, didn't do anything with it, the scuttlebutt, I don't know whether this is true or not, was that there was such concern that the corporations would react harshly to these carefully preserved tax breaks over the years being eliminated. And what I think has happened in the last year, if these hearings are any indication, is that corporations themselves are convinced that this system is broken.

Art Laffer: They are.

G. Russell Chaddock: They are pushing for changes. Getting rid of tax breaks. Perhaps not mine. Perhaps someone else's.

Art Laffer: And bring in the 3 trillion dollars abroad back.

G. Russell Chaddock: And the number they're settling on is that you could, without raising revenue neutral, bring it down to 28 percent. Thirty-five to twenty-eight. Now that's something that I've heard both Republicans and Democrats support. Is that worth putting in the middle ground?

Jared Bernstein: You know I think it is. I mean I think, again, revenue neutrality can't be your goal. I actually think you have to be revenue positive. But I do believe we're going to see corporate tax reform ideas, much like you just described. I'm a little more skeptical than you are about how business will react. From my experiences and talking to businesses about how this is gonna work. If you have a revenue neutral or revenue positive tax reform and you take down the rate, you broaden the base, somebody is going to get dinged. Someone will lose.

Now interestingly, when you're talking about the corporate rates, some of the biggest tax expenditures go to our manufacturers. There is a manufacturing production tax credit and there is an accelerated depreciation break. Those are the biggest corporate tax break in the industry side. Another very big one, very important to the financial market is the deductibility of debt finance through borrowing. Interest is interest finance – the interest payments that you pay on your debt financing are tax deductible. How would the financials feel about letting that go?

So I think what we're gonna see is the hypothesis you just laid out, we're gonna see that played out in coming weeks.

Art Laffer: The one thing I think we do disagree on, if I can, is that Jared sees the world much more statically then I do. I see it much more dynamic than you do. And I don't think anyone gets hurt by good tax reform, to be honest with you. Statically, of course, if you have it revenue neutral, equal number get hurt as get helped. But when you have dynamics all can get helped.

John Yemma: Okay. We're gonna go to questions. Bruce. Bruce is back and he's got questions from the audience.

Bruce Bond: I have a question first. Were you guys serious about writing a piece together?

Art Laffer: I was.

Jared Bernstein: I'm willing to give it a try. I'm willing to give it a try.

[Clapping]

Jared Bernstein: I will give it a try.

Bruce Bond: So I'm in the business world. I'd like a due date, please.

Jared Bernstein: I'm not gonna give you a due date.

Art Laffer: How about some time before Q2 ends. How's that? Is that fair?

Jared Bernstein: Maybe.

Bruce Bond: Jared, you're sounding like a political not an economist.

Jared Bernstein: J A R E D, by the way. Thank you. Yeah.

Bruce Bond: Alright. Well, we have some questions from the audience. And we got a lot of them. Unfortunately we're not gonna be able to go through all of them. But we're gonna go through a few. So there are a few here that really I think strike at the heart of how a lot of people feel out there in the electorate. And I'm gonna read a few of them.

The first one is as a 31 year old entrepreneur and investor I'm concerned about the future. How do higher taxes and potential tax hikes on high income earners incentivize me to work harder, expand my business, invest more in the markets and other business ventures?

John Yemma: What do you think? Jared?

Art Laffer: That's easy..

[Laughter]

Jared Bernstein: Yeah, no, that's -

John Yemma: It's a big one.

Jared Bernstein: That's what we've been talking about for the last 45 minutes. I can easily find for you, and maybe in my article with Art we'll try to find people on both sides, entrepreneurs who will tell you – Warren Buffett. Great example. Warren Buffett. I have a quote from Warren Buffett that I've used recently where he said – I'm doing the best I can to quote this. It may not be exact, but it's awfully close. And I think he's a guy who knows a little something about investing. I've never seen anyone – this is Buffett saying – in my whole career make a decision about investment based on the capital gains tax rate. They've made that investment based on their expected returns and without any consideration – he said, even when the capital gains tax rate was 40 percent. So while the question in the audience asks absolutely a reasonable question, I gotta tell ya, I talk to investors about this all the time. They just don't all feel that way. Many of them feel – you know in fact, what I would really like is a country that could educate its workforce, that could have reliable infrastructure, that could take care of its people. That's what a lot of business people really want.

[Clapping]

G. Russell Chaddock: There was an interesting comment from a FedEx executive at this hearing last week. He said we have to get back to basics where businesses make decisions based on products and services, not on what the tax code says. I think there's a kind of frustration in the gymnastics of getting through a tax code so dense that –

Jared Bernstein: I'm glad we're having a debate on tax reform. But I gotta tell you, we spend much too much time worrying about tax reform. What we really need to do is invest in our people and our nation. That simple.

Art Laffer: You got a lot of claps last time.

Jared Bernstein: No, I'm not looking for claps.

Bruce Bond: Alright. Let me go to the next question which is the Laffer curve seeks an outcome of more higher paying jobs. However, the reinvestment decisions are left to the beneficiaries of the tax breaks. How do you incentivize reinvestment rather than promote savings our outsourcing of capital?

Art Laffer: I'm gonna disagree with the first one. The beneficiaries of the tax rate reductions are not necessarily those people whose taxes are cut. You know the tax rates are reduced and what you have is more jobs, more output, more employment. And the true beneficiaries are people whose taxes may not have been changed at all. They're the ones who now have good high paying jobs rather than being unemployed. That's my first point there.

The second is these people should be doing it based on good economics and creating more jobs, more output, more employment. That's what dynamics is all about. And I do agree with Jared on – I mean there are certain functions of government we've gotta have. Not only do we have to have, we really need them and they're wonderful. I mean bridges, roads, all of this, education, no one disagrees with that.

John Yemma: What about safety nets?

Art Laffer: Safety nets to limits. I think 99 weeks unemployment is too long. I think in some of these areas where I did a lot of my – I wrote enterprise zones back in mid 70s, early 70s for the inner cities. What I did was I took a family of four going from 0 income to fifteen hundred dollars a month. And their actual spending power actually declined. Because they lost all their welfare payments. All their food stamps, all their supplemental security income, all the other stuff. By the way, not cheating at all. They literally were worse off at fifteen hundred dollars a month. That's when I did all the stuff with Reagan I did two things. I cut tax rates on the highest and I also got enterprise zones in there at the lowest. We could not get enterprise zones through Congress.

Audience Member: *[Inaudible]*

Jared Bernstein: No, it's the means testing.

Art Laffer: It's the means testing that does it, Larry. You have the tax rates are very high cause you lose all your social welfare benefits the more income you get.

Jared Bernstein: The minute you hit an income limit, your effective tax rate on something goes from 0 to 25 percent or something.

Audience Member: How do you get around that?

Jared Bernstein: Welfare cliff. You faze them out.

Art Laffer: I would do it by giving them lump sums. And you just let them keep the money. Period. For three years. And then –

Jared Bernstein: Like the earned income tax credit, which is actually a Reagan favorite. The earned income tax credit. Has a phase in and a long phase out. And I think that helps as well.

Art Laffer: But you do have a problem there, Larry. It is a real problem figuring these things out and making them work.

Jared Bernstein: Tax cliffs.

Art Laffer: It is really tough.

Bruce Bond: So there's a fundamental question relative to tax policy that is about its purpose. And a lot of different individuals look to the tax code to solve different problems. So this individual wants to know should tax policy be an investment of social policy or as a means of optimizing revenue for the government.

[Cross Talk]

Art Laffer: Well, I don't think it should be a means of optimizing. It should be a means of optimizing but not maximizing revenue for the government. You don't want to make it where you collect the maximum amount of revenue. And what you have to do is do it over a long period of time as well. You don't want to optimize for a week;you'd have to do it for a long horizon. But when you look at it that way I think it's really for social benefits that we do with the tax codes. And we do the infrastructure. We do the education. I'm not going to agree with Jared, at least as I heard him, now I'll say it a little different. Education is not just to get people employed and be skilled workers. Education is to also have a civilized society.

Jared Bernstein: I agree with that.

[Clapping]

Absolutely. No, my concern is that if we're going to keep collecting 15 percent of revenues, which is a current of GDP and revenues is the current number right now and historical average is more like 18, and continue to have the kind of dysfunction that Gail's been describing where revenues are off the table, we're not going to be able to supply the kinds of educated people in society. Having nothing to do with employment. And not to mention their infrastructure. We've got 100,000 public schools across this country, many of which suffered terrible maintenance backlogs. Even in rich communities like the – in Alexandria, Virginia. Affluent community. There are kids going to school in trailers. How does that make sense?

Art Laffer: I think you're really being a little unfair. I mean a little unfair to Tea Partiers. If I may say that. I don't think revenues are off the table at all. I think we're talking about growth and do you think you can really get growth by raising tax rates? And my view is that whenever we've raised tax rates –

Jared Bernstein: That's a fair point. No, it's a fair point.

Art Laffer: So the Tea Partiers really want the growth. They want more revenues. They just don't want higher rates.

John Yemma: But in the process of reform, Jared has said that he would favor revenue positive not just revenue neutral. What about you?

Art Laffer: I think we all would. I mean there's no benefit here to tax deductions loopholes and dodges and all that stuff. I mean if you can get those rates down enough, we need to have enough revenue to run government –

Jared Bernstein: He started by endorsing – hold on. He started by endorsing by Bowles Simpson.

Art Laffer: I thought I was pretty clear on that.

[Cross Talk]

Kraft Bell: There are common words you could use. Cause somehow when you talk static and dynamic it seems to create a gap between you.

Jared Bernstein: There is a gap.

Art Laffer: That is the honest gap between us.

Jared Bernstein: That is the biggest gap between us.

Art Laffer: That is really.

Jared Bernstein: I don't buy that dynamic mumbo jumbo.

Art Laffer: I don't buy his mumbo jumbo about static stuff.
Kraft Bell: That's why I brought it up. So my point is what is the common ground?

Art Laffer: We have lots of common ground, it's just not that one.

Jared Bernstein: Yeah, I mean it's the –

Kraft Bell: But if you've got a common ground on that one it would solve a lot of other -

[Cross Talk]

Art Laffer: That would make him vote for a Republican.

Jared Bernstein: If Art Laffer would agree with me, and the Congressional Budget Office, we would have common ground. And –

Art Laffer: If they'd ever been right I would agree with them.

[Laughter]

Art Laffer: Just teasing.

Jared Bernstein: No, I just don't – I

Kraft Bell: You're doing a good imitation of congress now. The question is, you said we need new people. You know the kind of people we need. If you sat there as new members of congress, how would you talk about this issue? What would you say to each other?

Jared Bernstein: We don't need to – I think it's a great question, by the way. I don't mean to dismiss it. Just think that we don't need – I don't think we need to agree on dynamic versus static scoring in order to –

Kraft Bell: That wasn't my question. My question is what is it that you should agree to that can move this issue forward?

Art Laffer: We have agreed on ten things here. Simplicity in the tax codes. Broadening the base and getting rid of that for fairness or whatever reason.

Kraft Bell: We've got all that documented. I'm just trying to stick with this one because it's like it's a cause somehow. It's like if you can say, I don't believe in dynamic and static. The question is there's gotta be a common ground somewhere in that that says that the world is not static, but it's not so dynamic that you can predict what everybody's gonna do. So what is the common ground for – how can we even analyze this so that we can come up with –

Jared Bernstein: I just don't think – look, I mean I don't know how far we agree or disagree. I mean it's funny, my good buddy and role model, Larry Kudlow's in the audience. It's always good to be with you, Larry. We were on a show the other night, on one of Larry's shows. And I was – let me just – so I think this would be helpful to you. I was arguing with Larry and another guest about – I think it was Newt Gingrich's tax plan. Which costs the treasury about 600 billion per year. And this other guest said, yeah, okay –

Art Laffer: Moi.

Jared Bernstein: Oh, was it you? Sorry.

Art Laffer: It was.

Jared Bernstein: I didn't think it was you.

Art Laffer: Yes, it was.

Jared Bernstein: Okay. So I was –

[Laughter]

Sorry. It would have been nicer if –

Art Laffer: But this other guest. Go ahead. I was waiting for it.

Jared Bernstein: I didn't have the monitor on. And I guess it was Art who said, yeah, it's 600 billion per year, Jared, but you're leaving out the dynamic effects. Well, 600 billion per year is about 4 percent of GDP. There is no dynamic model in the world that could possibly get you that kind of revenue. So if you want me to come to find a middle ground, I'll give – I might be able on a good day to give you 25 basis points –

Audience Member: I, by the way, asked Art the question because of my degree of incredulity on that –

Jared Bernstein: Okay, thank you.

Art Laffer: Now can I answer the question there? What I do believe is that there is another issue here. It's how much should be taxed. That is an issue. In this discussion, the tax codes, I personally go along with Simpson – not Mazzoli. God, that was the worst piece of legislation ever. But Simpson Bowles, which is good. I would surely go along with that. Would I rather see tax, total tax take come down by government spending being reduced? Yeah. I mean I really think the government spending in the last four or five years has caused the great recession. That's me. And I think the first thing is we don't have a deficit problem. I think we have a spending problem. Our tax codes are a problem. But not because they over collect or under collect. Our tax codes are a problem because they discriminate across the board. But we have a spending problem that I think is very, very serious.

John Yemma: So will you be relatively happy to see –

[Clapping]

Will you be relatively happy to see the super committee plan kick in at the end of the year and give these automatic cuts?

Art Laffer: You know I find the super committee thing is arbitrary. It – you know I don't know why they would make it this way. But, you know, I want to see cutting in spending. But you know how the super committee has done it I think is one of the most inane ways ever. Not that I disagree with this program or that program. It's over ten years, which is stilly to begin with. It's back end loaded, which means it's really meaningless there. And it also will be –

Jared Bernstein: I gotta say one thing about the spending. Cause I think people really misunderstand it. The increase in spending is completely related to the budget, to the great recession.

Art Laffer: Yes.

Jared Bernstein: The great recession led to a loss of wealth, of trillions of dollars when the housing bubble burst. And GDP is way below its potential trend. So we've lost tons of output, tons of jobs. And the thing about the budget deficit, the budget deficit is not driven by temporary spending. If you look at the contribution of the Recovery Act, 800 plus billion dollar Recovery Act to the budget deficit, by 2014 it's going to be less than half a percent of GDP in terms of its contribution to the budget deficit. Things that get in and out of the system have almost nothing to do with the long term budget deficit.

What drives the budget deficit right now are the Bush tax cuts. That's what's driving the budget deficit. Not Keynesian anti spending.

Art Laffer: Can I try answering a – am I allowed to –

John Yemma: We have another question.

Bruce Bond: Actually, Art, why don't you answer that and then we're gonna need to wrap up.

Art Laffer: See, I think it's the spending that caused the great recession. I think these temporary things –

[Clapping]

[Cross Talk]

Jared Bernstein: The housing bubble.

Art Laffer: If we have a two farm example. Farmer A and Farmer B. Alright. That's the whole world. If Farmer B gets unemployment benefits, who do you think pays for them? Am I going way over your heads on this? Government spending is –

Jared Bernstein: Not the farmers again. Not the farmers.

Art Laffer: Government spending is taxation pure and simple. And the stimulus spending we've had has not been just the 862 billion, which was your guys. It's 3 ¾ trillion. It's a year and a half pluses worth of all federal taxes. If you'd have asked me how to get out of the great recession and have the same amount of money, 3 ¾ trillion, I would have had a federal tax holiday on all federal taxes for a year and a half. And you'd have had the same budget position today. I'll tell you, we'd have sold cars into central China if we'd had no federal taxes.

Jared Bernstein: Unfortunately, the least effective part of the stimulus I think was the tax cuts.

Art Laffer: But those are tax cuts not tax rate cuts. That's the whole distinction I'm making here. There were no rate cuts in the budget. They were all inframarginals. They were tax cuts they called, which are really spending. It's like child credits and tax credits and stuff like that. That's not a tax rate reduction –

Jared Bernstein: So is there something we just kinda fundamentally disagree on. The cause of the great recession.

Art Laffer: That is. That is.

Jared Bernstein: I think it's well established that the causes of the great recession are housing bubble inflated by financial speculation. I don't think there's any question.

Bruce Bond: Well, I would just like to point out that while we have identified a few items where you do disagree, I think the audience would agree we found a lot of common ground tonight. And it's very gratifying to see this. I think all of us wish that if our public officials address this the way you all have done tonight; we'd be in a much better position than we are now.

John Yemma: Bruce, really quickly, I just wanted just as we close, maybe we'll ask each one of them if there's – they've surprised us in one way because they've basically agreed to this *Wall Street Journal* piece. Or possibly –

[Cross Talk]

Is there one thing though that –

Art Laffer: His friends won't like him anymore.

John Yemma: One thing that you want to surprise the audience with? Anything that you've been thinking about that is sort of, has either come out in your thinking here or that they don't know about?

Jared Bernstein: I guess I'd say one thing. You know a lot of the – in the document a lot of the rhetoric about increasing in taxes as all phrased on folks at the upper end of the income scale. And I know that the president has always said, you know tax increases should only be for people who's above 250,000. I actually don't think we can achieve the goals that I've set out in terms of an adequately funded government and the revenues that we need only if we're going to restrict any taxes to people at 250,000 or above. I think that the tax cuts of the Bush era ultimately have to sunset in completion. Not just the high end. But you can't do that right away. It's gonna take a phase in.

John Yemma: Okay. Art? Anything surprising there?

Art Laffer: No.

John Yemma: Okay. Bruce.

Bruce Bond: All right. Well, before we end, I wonder if we could have the house lights come up just a little bit. We have some questions for you in the audience. That's good. So the first question is you know what your position is on tax reform. Do you think as a result of tonight that you have a better understanding of the opposite side? Those who think yes you do, please raise your hand. I'm gonna guess, that looks like about 60 percent of you. That's a good number. Do you better understand – to what extent – let me ask the question differently. If you think you understand your own position better than you did before, please raise your hand. Maybe 30 percent of you.

How many of you out there have changed your mind on your position? Zero. Zero percent.

G. Russell Chaddock: Run for Congress.

Bruce Bond: You guys are very eloquent, but you're not good at evangelism. And how many of you here in the audience feel that some progress was made tonight? Oh, my goodness, that's about 85 percent maybe. That's a great number. Well, thank you for that insight. I think all of you would feel the same way I do about what a wonderful panel we had tonight. Why don't we all give all of the panelist, Gail, John, Art –

[Clapping]

[End of Audio]